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Ms. Marlene Dortch
Secretary
Federal Communications Commission
445 12th Street, SW, Room TWB-204
Washington, DC 20554

Re: Notice of Written Ex Parte Communication, In the Matter of Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, CC Docket Nos. 01-338, 96-98 and 98-147

Dear Ms. Dortch:

The purpose of this letter is to demonstrate that resale of local services under the limited provisions of the Telecommunications Act of 1996, often referred to as Total Service Resale ("TSR"), is patently insufficient to support an effectively competitive market for mass-market services, *i.e.*, services used by residential and small business customers that are served by voice grade loops. In particular, this letter highlights the fact that the TSR-based local services that can be offered pursuant to the narrowly circumscribed terms of sections 251(c)(4) and 252(d)(3) of the Act are completely different from the broad market-based resale of long distance services that helped to generate – and still supports -- vibrant competition in the long distance market. Indeed, the market-based resale that supported long distance competition is much closer to UNE-P, *not* the limited and ineffectual competition supported by TSR. As I explain below, were resale available in the local market as it was and remains in the long distance market, it would generate resale discounts on the order of 65% or more, rather than the discounts of about 20% that have been proven inadequate during the last seven years. Even then, resale could not foster the same level of consumer benefits as UNE-P, which offers broader opportunities for service differentiation and new offerings.

As a threshold matter, recent *ex partes* filed by other carriers have demonstrated that many of the myths regarding the relationship between UNE-P and TSR are simply unfounded. In particular, a recent CompTel *ex parte*[1] shows in detail that UNE-P is *not* the

[1] *Ex parte* letter from Maureen Flood dated November 18, 2002.

same as TSR because, among other things, TSR limits a competitor to the exact retail offers of the incumbent.

In contrast, UNE-P enables competitors to develop different calling plans, billing capabilities and feature packages than the ILEC, and it also enables competitors to differentiate their services through investment in new technology. For example, with UNE-P, AT&T introduced an extended IntraLATA calling plan in New York, and a substantial percentage of our New York customers have selected this plan. AT&T has also recently introduced extended IntraLATA plans in California, Michigan, Illinois, Ohio and New Jersey, and also offers innovative 3-feature bundles that may offer customers more value than would be feasible if AT&T had to individually purchase each feature from the ILEC at a resale discount. If AT&T and other CLECs are forced to acquire and/or serve our customers via resale, local customers would likely lose the benefit of these offers and see little future innovation or simplification in calling plan design.

Similarly, CompTel's *ex parte* shows that competitors do not use UNE-P simply to mimic ILEC services. Rather, they have in fact used UNE-P to provide additional service options in many states across the country. Finally, it shows that UNE-P competition is real, in that it is the only entry vehicle that has been able to generate competition on over 10 million mass-market lines in a manner that offers consumers the prospect of real savings, both through lower prices offered by CLECs and competitive responses from the incumbents.[2]

AT&T's own experience proves that TSR is a hugely unprofitable entry strategy in local markets. Indeed, AT&T lost *billions* of dollars in attempting to provide a TSR-based offer to mass-market customers. There are two key reasons why TSR has failed to support competition in local markets while long distance resale was so successful in promoting and sustaining long distance competition. The first relates to the types of local services that are legally and practically available for resale. The second is the discounts available to local versus long distance competitors.

Limited Services Available for Resale - Section 251(c)(4)(B) allows the imposition of service restrictions on the use of resold services. More specifically, that section provides that a PUC may "prohibit a reseller that obtains at wholesale rates a telecommunications service that is available at retail only to a category of subscribers from offering such service to a different category of subscribers." In sharp contrast, the Commission's long distance resale rules do not permit such restrictions. Thus, a long distance reseller can purchase very high volume services that have been designed for sale to the largest business customers (and thus carry the highest volume discounts) and resell them as retail services to small long distance users. Indeed, that is the very entry strategy that RBOCs are using as they enter the interLATA market. Such deep discounts – which approach 65% or more – combined with the electronic PIC "equal access" process, enable them to enter the long distance market quickly and easily with hugely successful results. Indeed, Verizon has just announced (i) that it has become the nation's third largest long

[2] *See also* CompTel Press Release dated January 7, 2003 "Competition Could Save Consumers Up To $9.25 Billion In Local Phone Bills, CompTel Says" ("CompTel Press Release").

distance carrier, with over 10 million lines in service in 47 states, (ii) that customer research shows that 11% of households with long distance charges use Verizon and (iii) that "Verizon's strategy has been to use long-distance service as a linchpin in its approach to the consumer market."[3] And Verizon has achieved all this largely as a reseller of other carriers' long distance services and networks. TSR, by contrast, has only been able to support trivial competition in the local services market for the very same customers. Moreover, Verizon's total of long distance lines alone – not counting the long distance services offered by other RBOCs in the past two years - is the rough equivalent of the *total* number of local lines that *all* CLECs have been able to capture using UNE-P in the nearly seven years since the Act was passed.[4]

Equally important, local services for large business customers are provided over high-capacity facilities that use DS-1 and higher level loops to provide dedicated connections between large customers' premises and the ILEC's serving office. Those services are simply not available to competitors who seek to use TSR to serve mass-market customers, because such customers (i) require only voice-grade loops and (ii) need their own dedicated connections between their premises and the incumbents serving office.

TSR Offers Commercially Insignificant Discounts - Nor is there any similarity between the resale discounts permitted under TSR and those available to long distance resellers. TSR discounts are highly circumscribed by section 252(d)(4), and apply only to the "marketing, billing, collection and other costs that will be avoided" by the ILEC. This is a far cry from the discounts that have been available to long distance resellers – including the RBOCs. Long distance resale discounts are based on market forces and market arbitrage, *not* narrowly circumscribed regulatory rules. Thus, long distance resellers could buy services for resale at prices close to cost, even when there was only a single provider, because the discounts available to the largest users could be used to provide service to the smallest consumers.

The situation is totally different for TSR. The statutory standard for establishing the TSR discount only reduces the reseller's costs by the ILEC's actually avoided retailing costs. Thus, it has *no effect at all* on the ILEC's margins from providing its services. Indeed, the statutory standard *assures* that the ILEC will retain its *entire profit* on the monopoly services subject to TSR. Moreover, as shown above, the services subject to the TSR discount are *not* the highly discounted, high-volume business services that serve as the basis for the long distance resellers' retail prices. Rather, they are the highest priced retail services available to the smallest users. Thus, TSR discounts, by definition, exert absolutely no market discipline over the prices that consumers must pay for their local services. Such discipline can only occur if competitors have access to the inputs to their retail services at costs that are comparable to the ILEC's costs. And that result can only be attained if CLECs have access to UNE-P.[5]

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[3] Verizon news release available at www.newscenter@verizon.com (also announcing

[4] *See ex parte* filed on behalf of PACE et al., dated January 16, 2003 ("PACE *ex parte*").

[5] There is also another critical difference between the competition generated under the long distance regime and current efforts to bring competition to local markets. In the former, competitors were provided steep discounts on access charges while they had inferior access to customers compared to the incumbent. In local

Market experience validates this fact. Because of the practical and economic limitations on TSR, it has been able to generate at best trivial competition. On the other hand, as PACE and others have shown, UNE-P, has been the main growth engine for local competition and lower consumer prices for local service.

In sum, there is absolutely no doubt that TSR-based competition cannot generate meaningful competition for mass-market local customers. In the current market environment – especially in the absence of an electronic means for transferring consumers' loops -- the only entry vehicle that can support meaningful local competition for the vast majority of American consumers is UNE-P.

Consistent with Commission rules, I am filing one electronic copy of this notice and request that you place it in the record of the above-referenced proceedings.

Sincerely,

Joan Marsh

cc: William Maher
Jeff Carlisle
Michelle Carey
Brent Olson
Rich Lerner
Scott Bergmann
Thomas Navin
Jeremy Miller

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markets, however, the record is now undisputed that CLECs face the penalty of appreciable *additional* costs in using their own facilities to provide service to the lowest volume customers. *See* SBC *ex parte* dated January 14, 2003, acknowledging significant additional costs per line per month for CLECs that provide POTS using their own switches.